

# PRAJ INDUSTRIES

## FY18 challenging; growth visibility revving up

India Equity Research | Engineering and Capital Goods

FY18 was challenging for PRAJ as dip in ethanol revenues dented profitability and order intake grew mere 5%. Going ahead, as 2G orders gain momentum (mostly domestic OMC), the company's FY19/20 new order intake could get a significant leg up. Also, recent management change—Mr. Shishir Joshipura appointed MD & CEO—we believe could be a key turning point in Praj's growth story given his excellent track record. We expect the company's order inflow to clock 16% CAGR over FY18-20E led by pick up in 2G ethanol orders, apart from a reasonable 20% growth (on a low base) in the hi-purity business, which is another high-potential growth avenue. Maintain 'BUY' with TP of INR115 (26x FY20E EPS) given improving growth visibility and profitability.

### Adverse mix impacts margin

Q4FY18 revenue declined 9% YoY largely due to absence of any major execution during this quarter of orders in hand. Ethanol business declined 25% YoY on back of weak opening order book. Adverse revenue mix (higher share of engineering/brewery segment) continued to impact EBITDA margin—down 280bps YoY to 9.9%. On a conservative basis, management has excluded INR1.75bn of slow-moving orders from the order book, resulting in a closing order book of INR6.75bn (down 28% YoY).

### 2G ethanol ordering to gather pace in FY19/20E

Post the HPCL order bagged in Q3FY18, Praj has now successfully bagged IOCL's INR387mn order for the 2G bio-refinery project located in Panipat. While OMCs' service orders for 2G ethanol plants have started gathering pace, we expect ordering to pick up for critical / non-critical equipment over ensuing quarters, driving 16% order inflow CAGR over FY18-20.

### Outlook and valuations: Bright prospects; retain 'BUY'

We expect profitability to ramp up led by pick up in 2G ethanol business and estimate 40% earnings CAGR over FY18-20. Deferment of 2G ethanol ordering by OMCs and probable change in the bio-fuel policy in the backdrop of possible government change continue to remain key risks to our estimates. At CMP, the stock trades at 32x/22x FY19/20E EPS. We maintain 'BUY'.

#### EDELWEISS RATINGS

Absolute Rating	BUY
Investment Characteristics	Growth

#### MARKET DATA (R: PRAJ.BO, B: PRJ IN)

CMP	: INR 99
Target Price	: INR 115
52-week range (INR)	: 132 / 61
Share in issue (mn)	: 181.0
M cap (INR bn/USD mn)	: 18 / 264
Avg. Daily Vol. BSE/NSE ('000)	: 1,595.2

#### SHARE HOLDING PATTERN (%)

	Current	Q3FY18	Q2FY18
Promoters *	33.3	33.4	33.5
MF's, FI's & BKs	18.7	19.5	21.7
FII's	13.2	12.3	9.6
Others	34.8	34.8	35.2
* Promoters pledged shares (% of share in issue)	:	NIL	

#### PRICE PERFORMANCE (%)

	BSE Midcap Index	Stock	Stock over Index
1 month	(4.2)	4.8	9.1
3 months	(3.5)	7.1	10.6
12 months	6.3	20.3	14.0

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#### Financials

(INR mn)

Year to March	Q4FY18	Q4FY17	% Chg	Q3FY18	% Chg	FY18	FY19E	FY20E
Net revenues	2,745	3,016	(9.0)	2,483	10.6	9,166	10,518	12,314
EBITDA	271	383	(29.4)	168	61.1	610	894	1,268
Adjusted Profit	228	228	0.0	76	200.9	395	547	784
Diluted EPS	1.3	1.3	0.0	0.4	200.9	2.2	3.1	4.4
Diluted P/E (x)						44.4	32.1	22.4
EV/EBITDA (x)						24.4	17.0	12.0
ROAE (%)						5.5	7.5	10.4

### Q4FY18 conference call: Key highlights

#### Industry:

- The Indian cabinet approved bio-fuel policy. Viability funding of INR50bn over the next six years in addition to additional tax incentives and higher purchase price have been indicated in the policy.
- European Union: Discussions underway for increased use of ethanol in the transportation sector.
- Vietnam is moving towards 5% blending. Argentina, Colombia and Peru are targeting higher blend ratios as well.
- Growth in Thailand continues to remain healthy.

#### Financial performance:

- Revenue impacted by timing of order intake during previous quarters. Domestic revenue contributed 64% to revenue.
- EBITDA margin impacted by adverse sales mix.
- **Order intake:** INR3.75bn. IOC has awarded Letter of Acceptance for a wider scope of license of proprietary technology, design package and project management (EPCM) for INR387mn.
- **Order book:** INR8.5bn. However, excluding the slow-moving orders of INR1.75bn, order book stands at INR6.75bn.
- Capex in FY18: INR 160mn.
- Execution is on track for the BPCL 2G ethanol service order bagged in Q3FY18.
- BPCL and IOC orders for equipment are likely to be awarded over the next two-three months.

#### Other comments:

- **Petrobas order:** Kero signed order in March 2018. Now ordering for equipment from Kero to start soon in which Praj will participate.
- Praj is getting approval to supply critical equipment to large suppliers to drive growth ahead. E.g., one equipment being supplied in the US.
- General order size—critical equipment (INR1.5-2.0bn) and non-critical equipment (INR2.0-2.5bn).
- Successfully delivered on high complex jobs in chemical and oil & gas sectors.
- Municipal solid waste to bio gas is on the agenda, which is likely to be developed over the next two-three years.
- Feedstock pricing is region specific.

Financial snapshot						(INR mn)		
Year to March	Q4FY18	Q4FY17	% change	Q3FY18	% change	FY18	FY19E	FY20E
Net revenues	2,745	3,016	(9.0)	2,483	10.6	9,166	10,518	12,314
Raw material costs	1,372	1,632	(15.9)	1,353	1.4	4,693	5,364	6,157
Staff costs	392	333	17.8	354	10.9	1,495	1,630	1,872
Other operating expenses	711	668	6.5	608	16.9	2,368	2,629	3,017
Total expenditure	2,475	2,633	(6.0)	2,315	6.9	8,556	9,624	11,046
EBITDA	271	383	(29.4)	168	61.1	610	894	1,268
Depreciation	61	54	12.9	61	(1.3)	241	271	286
EBIT	210	330	(36.3)	107	97.0	369	623	983
Other income	101	40	152.9	16	551.0	172	202	200
Interest	3	2	50.0	3	(6.3)	11	8	12
Add: Exceptional items	40	-	-	-	-	-	-	-
Profit before tax	348	368	(5.3)	119	192.9	530	817	1,171
Tax	80	140	(42.7)	43	85.4	135	269	386
Minority interest								
Reported net profit	268	228	17.7	76	254.2	395	547	784
Adjusted Profit	228	228	0.0	76	200.9	395	547	784
Equity capital(FV INR 2)	362	362		362		362	362	362
No. of shares (mn)	181	181		181		181	181	181
Diluted EPS (INR)	1.3	1.3	0.0	0.4	200.9	2.2	3.0	4.3
<b>As % of revenues</b>								
Raw material	50.0	54.1		54.5		51.2	51.0	50.0
Employee cost	14.3	11.0		14.2		16.3	15.5	15.2
Other expenses	25.9	22.1		24.5		25.8	25.0	24.5
EBITDA	9.9	12.7		6.8		6.7	8.5	10.3
Depreciation	2.2	1.8		2.5		2.6	2.6	2.3
Other income	3.7	1.3		0.6		1.9	1.9	1.6
Adjusted net profit	8.3	7.6		3.0		4.3	5.2	6.4
Tax rate	23.0	38.0		36.3		25.5	33.0	33.0

### Company Description

Praj, since inception in 1984, has evolved from a dominant, single business enterprise into a global organisation driven by technology innovation and integration capabilities in process engineering and industrial biotechnology domains. As its core business, the company offers innovative technology solutions and project implementation and management services to the bio-ethanol industry. It is also involved in two major growth platforms—one focusing on industrial solutions for water & waste water management and critical process equipment & systems and the other on bio-based products. A globally leading company with over 600 references in more than 60 countries across five continents, Praj has acquired an international repute for responsible and reliable solutions. Having established a global leadership in first generation ethanol technology, Praj has initiated a project to expand its 2G Cellulosic Ethanol Program to demo scale. Praj has well equipped manufacturing facilities—one in Pune and two at Kandla (Gujarat) port of India and another at Wada near Mumbai.

### Investment Theme

#### **Diversification to high growth segments imparts scalability**

Praj has diversified its revenue base over the past four-five years with core business contribution moving from 100% to 72% currently; emerging businesses—critical process equipment, waste water, Neela—contribute the balance. The company aims to further improve overall revenue mix to 50:50 by FY18E led by stable growth in conventional and high growth (25% CAGR) in emerging businesses.

#### **Core business steady; brewery business gaining traction**

Led by global references and ethanol blending mandates in key export regions like US, Brazil, Columbia, Peru, Thailand, Malaysia etc, Praj has sustained a steady position in the global ethanol market. Its brewery business recently bagged two large projects overseas and expects to sustain the increased momentum.

### Key Risks

**Regulatory mandate:** A large part of Praj's business (~55% ethanol business) comes from regulatory mandate. Any delay or change in the decision of the government could impact the business adversely.

**Slowdown in industrial capex:** Any slowdown in industrial capex and consumption may impact revenue and hence the company's profit.

**Letdown of the 2G plant:** While we have not built any financial impact of 2G plant commercialisation, we believe a lot of hopes have been pinned around the success of 2G plant. Any failures to compete with the global players might dampen the investor's sentiments.

## Financial Statements

### Key Assumptions

Year to March	FY17	FY18	FY19E	FY20E
<b>Macro</b>				
GDP(Y-o-Y %)	6.6	6.5	7.1	7.6
Inflation (Avg)	4.5	3.6	4.5	5.0
Repo rate (exit rate)	6.3	6.0	6.0	6.5
USD/INR (Avg)	67.1	64.5	66.0	66.0
<b>Company</b>				
Revenue growth (%)				
A) Ethanol business	(19.3)	(10.9)	12.8	29.5
B) Brewery business	(1.6)	114.1	44.4	(6.4)
C) Emerging business	12.6	(41.2)	(25.1)	34.9
Order intake growth (%)				
A) Ethanol business	5.7	(16.6)	31.6	25.0
B) Brewery OI growth	(28.9)	337.8	(20.0)	10.0
C) Emerging business	(4.8)	(49.4)	20.0	20.0
Dep. (% gross block)	5.6	5.7	5.7	5.7
Tax rate (%)	33.9	33.0	33.0	33.0

### Income statement

(INR mn)

Year to March	FY17	FY18	FY19E	FY20E
Income from operations	9,150	9,128	10,478	12,300
Materials costs	4,671	4,745	5,344	6,150
Employee costs	1,480	1,471	1,624	1,870
Other mfg expenses	2,266	2,345	2,619	3,014
Total operating expenses	8,418	8,562	9,587	11,033
EBITDA	732	566	891	1,267
Depreciation	221	242	261	275
EBIT	511	324	630	992
Add: Other income	177	182	195	205
Less: Interest Expense	13	12	19	29
Profit Before Tax	675	494	806	1,168
Less: Provision for Tax	229	163	266	385
Reported Profit	446	331	540	782
Adjusted Profit	446	331	540	782
Shares o /s (mn)	177	177	177	177
Adjusted Basic EPS	2.5	1.9	3.0	4.4
Diluted shares o/s (mn)	177	177	177	177
Adjusted Diluted EPS	2.5	1.9	3.0	4.4
Adjusted Cash EPS	4.0	3.2	4.5	6.0
Dividend per share (DPS)	1.8	2.0	2.2	2.4
Dividend Payout Ratio(%)	82.7	122.6	82.7	62.8

### Common size metrics

Year to March	FY17	FY18	FY19E	FY20E
Operating expenses	92.0	93.8	91.5	89.7
Materials costs	51.1	52.0	51.0	50.0
Staff costs	16.2	16.1	15.5	15.2
Other mfg expenses	24.8	25.7	25.0	24.5
Depreciation	2.4	2.7	2.5	2.2
Interest Expense	0.1	0.1	0.2	0.2
EBITDA margins	8.0	6.2	8.5	10.3
Net Profit margins	4.9	3.6	5.2	6.4

### Growth ratios (%)

Year to March	FY17	FY18	FY19E	FY20E
Revenues	(9.9)	(0.2)	14.8	17.4
EBITDA	(32.0)	(22.7)	57.3	42.3
Adjusted Profit	(40.1)	(25.8)	63.0	44.9

## Engineering and Capital Goods

Balance sheet		(INR mn)			
As on 31st March	FY17	FY18	FY19E	FY20E	
Share capital	359	359	359	359	
Reserves & Surplus	6,738	6,663	6,756	7,047	
Shareholders' funds	7,096	7,021	7,115	7,406	
Minority Interest	3	3	3	3	
Short term borrowings	43	143	243	343	
Long term borrowings	1	1	1	1	
Total Borrowings	43	144	244	344	
Long Term Liabilities	158	159	159	159	
Deferred tax (net)	(109)	(109)	(109)	(109)	
<b>Sources of funds</b>	<b>7,192</b>	<b>7,218</b>	<b>7,411</b>	<b>7,802</b>	
Gross Block	4,018	4,268	4,518	4,768	
Net Block	1,936	1,943	1,932	1,907	
Capital work in progress	315	325	335	345	
Intangible Assets	626	626	626	626	
Total Fixed Assets	2,876	2,894	2,893	2,878	
Non current investments	137	147	157	167	
Cash and Equivalents	2,079	2,132	2,140	2,250	
Inventories	1,045	1,040	1,171	1,348	
Sundry Debtors	2,949	3,023	3,445	4,044	
Loans & Advances	62	69	77	87	
Other Current Assets	2,617	2,748	2,885	3,030	
Total current assets	6,673	6,881	7,579	8,508	
Trade payable	2,134	2,171	2,445	2,814	
Other Current Liab	2,439	2,665	2,914	3,188	
Total Current Liab	4,574	4,837	5,359	6,002	
Net current assets	2,100	2,045	2,221	2,508	
<b>Uses of funds</b>	<b>7,192</b>	<b>7,218</b>	<b>7,411</b>	<b>7,802</b>	
BVPS (INR)	40.0	39.6	40.1	41.7	

Free cash flow		(INR mn)			
Year to March	FY17	FY18	FY19E	FY20E	
Reported Profit	446	331	540	782	
Add: Depreciation	221	242	261	275	
Interest (Net of Tax)	9	8	13	20	
Others	(9)	(8)	(13)	(20)	
Less: Changes in WC	407	(55)	176	287	
Operating cash flow	260	628	625	771	
Less: Capex	367	260	260	260	
<b>Free Cash Flow</b>	<b>(106)</b>	<b>369</b>	<b>365</b>	<b>511</b>	

Cash flow metrics				
Year to March	FY17	FY18	FY19E	FY20E
Operating cash flow	260	628	625	771
Investing cash flow	(267)	(270)	(270)	(270)
Financing cash flow	(483)	(306)	(347)	(391)
Net cash Flow	(489)	53	8	109
Capex	(367)	(260)	(260)	(260)
Dividend paid	(369)	(406)	(447)	(491)

Profitability and efficiency ratios				
Year to March	FY17	FY18	FY19E	FY20E
ROAE (%)	6.5	4.7	7.6	10.8
ROACE (%)	9.9	7.1	11.4	15.8
Debtors Days	132	119	113	111
Payable Days	164	166	158	156
Cash Conversion Cycle	48	34	31	30
Current Ratio	1.9	1.9	1.8	1.8
Gross Debt/EBITDA	0.1	0.3	0.3	0.3
Gross Debt/Equity	-	-	-	-
Debt/Equity (x)	-	-	-	-
Interest Coverage Ratio	39.0	26.6	32.5	33.7

Operating ratios				
Year to March	FY17	FY18	FY19E	FY20E
Total Asset Turnover	1.3	1.3	1.4	1.6
Fixed Asset Turnover	4.5	4.7	5.4	6.4
Equity Turnover	1.3	1.3	1.5	1.7

Valuation parameters				
Year to March	FY17	FY18	FY19E	FY20E
Adj. Diluted EPS (INR)	2.5	1.9	3.0	4.4
Y-o-Y growth (%)	(40.1)	(25.8)	63.0	44.9
Adjusted Cash EPS (INR)	4.0	3.2	4.5	6.0
Diluted P/E (x)	39.3	53.0	32.5	22.4
P/B (x)	2.5	2.5	2.5	2.4
EV / Sales (x)	1.7	1.7	1.5	1.3
EV / EBITDA (x)	21.2	27.5	17.6	12.3
Dividend Yield (%)	1.8	2.0	2.2	2.4

## Additional Data

### Directors Data

Mr. Pramod Chaudhari	Executive Chairman	Mr. Shishir Joshipura	CEO and MD
Mr. Sachin Raole	CFO & Director - Finance & Commercial	Ms. Mrunalini Joshi	Directors (Non-Executive)
Mr. Berjis Desai	Directors (Non-Executive)	Mr. Daljit Mirchandani	Directors (Non-Executive)
Mrs. Parimal Chaudhari	Directors (Non-Executive)	Mr. Rajiv Maliwal	Directors (Non-Executive)
Mr. Sivaramakrishnan S. Iyer	Directors (Non-Executive)		

Auditors - M/s P.G. Bhagwat

### Holding – Top10

	Perc. Holding		Perc. Holding
Chaudhari pramod m	21.38	Chaudhari pramod m	21.38
Chaudhari parimal	11.93	Chaudhari parimal	11.93
Hdfc asset managemen	8.84	Hdfc asset managemen	8.84
Tata cap financial s	7.41	Tata cap financial s	7.41
Sundaram asset manag	6.4	Sundaram asset manag	6.4

*\*as per last available data*

### Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
23 Nov 2017	Paramount Fintrade Pvt Ltd	Buy	367846	105.17

*\*as per last available data*

### Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
28 Feb 2018	Ghanshyam Deshpande	Sell	21000.00
02 Aug 2017	Dattatraya NimbolkarDATTATRAYA NIMBOLKAR	Sell	33340.00
27 Jul 2017	SANJAY KULKARNI	Sell	33340.00
24 Jul 2017	ABHIJIT DANI	Sell	15997.00
19 Jul 2017	vikram pandit	Sell	33000.00

*\*as per last available data*

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## Coverage group(s) of stocks by primary analyst(s): Engineering and Capital Goods

ABB India, Bharat Heavy Electricals, Bharat Forge, CG Power and Industrial Solutions, Engineers India Ltd, Greaves Cotton, KEC International, Cummins India, Kalpataru Power, Larsen & Toubro, Praj Industries, Ramkrishna Forgings, Siemens, TD Power Systems, Techno Electric & Engineering, Thermax, Triveni Turbine, VA Tech Wahab

### Recent Research

Date	Company	Title	Price (INR)	Recos
15-May-18	<b>KEC International</b>	Ending the year with a bang; visibility comforting; <i>Result Update</i>	381	Buy
14-May-18	<b>Larsen &amp; Toubro</b>	Reengineering core: A case for perception change; <i>Company Update</i>	1,382	Buy
11-May-18	<b>Siemens</b>	Innovation Day 2018: Expanding Industry 4.0	1038	Hold

### Distribution of Ratings / Market Cap

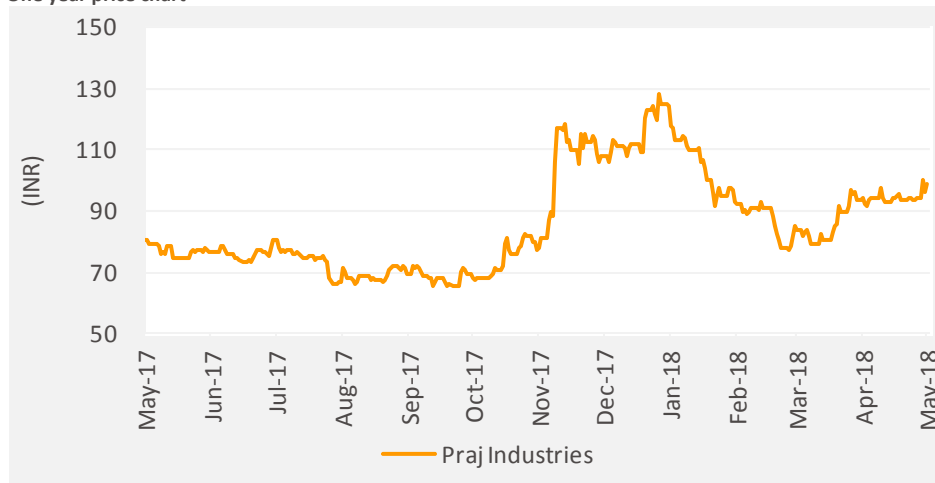
#### Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

#### Rating Interpretation

Rating	Expected to
<b>Buy</b>	appreciate more than 15% over a 12-month period
<b>Hold</b>	appreciate up to 15% over a 12-month period
<b>Reduce</b>	depreciate more than 5% over a 12-month period

One year price chart





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